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IN THE

Supreme Court of the United States

October Term, 1975

No. 75-354

THE FIRST BOSTON CORPORATION,
Petitioner,

v.

CHRIS-CRAFT INDUSTRIES, INC., *et al.*,
Respondents.

MOTION OF SECURITIES INDUSTRY ASSOCIATION FOR LEAVE TO FILE A BRIEF AS *AMICUS CURIAE* IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI, AND BRIEF IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI

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Pursuant to Rule 42 of the Rules of the Supreme Court of the United States, the Securities Industry Association ("SIA") hereby moves for leave to file a brief as *amicus curiae* in support of the petition for a writ of certiorari of The First Boston Corporation ("First Boston"). This motion is necessary because Chris-Craft Industries, Inc. refused to consent to the filing of an amicus brief by SIA.

The SIA was formed in 1972 through the merger of the Association of Stock Exchange Firms and the Investment Bankers Association of America. The SIA has approximately 700 members from all parts of the United States, all of whom are engaged in the securities business. The SIA is generally recognized as spokesman for the securities industry to the public and to the Government.

The April 11, 1975 decision of the Second Circuit Court of Appeals in this litigation for the first time held that a dealer manager in an exchange offer (and statutory underwriter) would be liable for an amount in excess of the total price of the securities distributed to the public pursuant to the offer. As the effect of this decision is to repeal portions of Section 11 of the Securities Act of 1933 and substitute unlimited, court-imposed liability (in this case amounting to one-half of the net worth of the investment banker), the decision is of great concern to the securities industry.

Through the attached brief, the SIA wishes to point out to the Court the grave consequences to the securities industry of the Second Circuit's decision, and to emphasize the legal issues which are applicable to the securities industry as a whole. The SIA therefore respectfully prays that the Court grant this motion for leave to file its brief in support of First Boston's petition.

Respectfully submitted,

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BRIEF OF SECURITIES INDUSTRY ASSOCIATION, *AMICUS CURIAE*, IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI

This Brief is submitted on behalf of the Securities Industry Association ("SIA") as *amicus curiae* in support of the petition for a writ of certiorari filed by The First Boston Corporation ("First Boston"). The issues that are raised by the unprecedented damage award levied against First Boston are important not only to investment bankers but to all parties in the capital formation process, and the SIA strongly believes these issues merit the attention of the Court.

The SIA was formed in 1972 through the merger of the Association of Stock Exchange Firms and the Investment

Bankers Association of America. The SIA is generally recognized as spokesman for the securities industry to the public and to the government.

Statement of the Case

First Boston was the dealer manager for an exchange offer, for which it received a fee of $40,000. Although the plaintiff, Chris-Craft Industries, Inc. ("Chris-Craft"), acquired no securities through the exchange offer, the Court of Appeals held First Boston jointly and severally liable to Chris-Craft for an amount exceeding $35,000,000. The sole basis of First Boston's liability was the good faith omission from the registration statement prepared for the exchange offer of the fact that the issuer had received and was considering an offer for an asset which was substantially lower than the carrying value of the asset.

While granting the SEC equitable relief (D1-21),[1] the District Court denied Chris-Craft relief on all of its claims against several defendants, including its attack on the registration statement (A125-162). As to First Boston, the Court found it had "acted solely" in "good faith" and accordingly found no basis for liability (A158-159).

The Court of Appeals reversed (A1-124), holding First Boston liable to Chris-Craft because it "did not adequately perform its duty" (A51) as an underwriter under Section 11 of the Securities Act of 1933 ("The 1933 Act"). The court held that First Boston owed this duty not merely to purchasers of the underwritten securities, but to Chris-Craft as well (A55).

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[1] The opinions below are reproduced in Joint Appendices A through E submitted with First Boston's petition. The page references herein are to that volume.

On remand, in response to the Court of Appeals' directive to determine "the reduction in the appraisal value" (A69) of Chris-Craft's shareholding in Piper Aircraft Corporation ("Piper"), the District Court found after trial that this reduction in appraisal value was $1,673,988 (B70). Prejudgment interest was also allowed (B76-79).

The Court of Appeals again reversed, however, saying that by "reduction in the appraisal value" it meant a rescission measure of damages, formulated as the difference between Chris-Craft's purchase price of the Piper shares and the price at which it could have sold such shares at a subsequent date (B25-31). Because of the decline in the market during this period, the court fixed the hypothetical sales price at a figure less than half the purchase price. The court thus awarded Chris-Craft damages of $25,793,365 (B31) and approximately $10,000,000 in prejudgment interest (B32-34).

The following important issues are raised by the opinions of the Court of Appeals:

1. Should the special "duty" and "absolute liability" imposed upon an underwriter of registered securities by Section 11 of the 1933 Act be implied under Section 14(e) of the Securities Exchange Act of 1934 ("The 1934 Act") in favor of parties to whom the registration statement was not addressed?

2. May a statutory underwriter be held liable under Section 14(e) for damages far in excess of the maximum permitted by Congress under Section 11 of the 1933 Act for the same conduct?

3. Should damages against multiple defendants be assessed on a joint and several basis in a case where the violations of the securities laws are separate and

distinguishable, without regard to the respective roles of each defendant?

Argument

I.

This Case Presents Important Questions With Respect to the Application of the Federal Securities Laws to Contests for Corporate Control and to the Duties Owed Non-Purchasers by Underwriters.

The Court of Appeals held that an unsuccessful contestant for corporate control has an implied right of action for damages under Section 14(e) of the 1934 Act. The decision has led to substantial uncertainty in the investment community both as to the basis upon which recovery can be had in such actions and as to the exposure to damages of professional advisors, such as First Boston, who are joined as collateral parties.

Congress did not intend "to discourage take-over bids" by passing the Williams Act, of which Section 14(e) was a part. *Rondeau* v. *Mosinee Paper Corp.*, 95 S. Ct. 2069, 2076. The decision below, however, will necessarily have that effect because it will fuel the already inevitable litigation that accompanies every battle for control, as the losers in the marketplace seek to secure consolation prizes in the form of huge damage awards.

The decision of the Second Circuit here also conflicts with the decision of the Fifth Circuit in *Sargent* v. *Genesco*, 492 F.2d 750 (5th Cir. 1974), in which the Court stated:

> "The evil to be remedied was inadequate disclosure to tendering security holders. Congress made it clear that the investor protection sought by 14(e) was disclosure to those who had to make the hold or sell decision." 492 F.2d at 769.

The Court then held "[n]o violation of 14(e) could be shown where the class sought to be protected has not been harmed." 492 F.2d at 769.

By expanding their exposure to legal liability far beyond any previous bounds, the decision below will inevitably deter investment banking firms and other professionals from acting as advisors to competing offerors. The assessment of damages of such magnitude should be given special scrutiny in light of Chief Judge Cardozo's caution in *Ultramares Corp.* v. *Touche,* 255 N. Y. 170, 179-80 (1931), that the "hazards of a business conducted" on terms of exposure to "liability to an indeterminate class" are "so extreme as to enkindle doubt whether a flaw may not exist in the implication of a duty that exposes to these consequences."

This Court in *Blue Chip Stamps* v. *Manor Drug Stores,* 95 S. Ct. 1917, has limited the exposure to liability of the principals as well as their advisors under Section 10(b) of the 1934 Act; the present case provides similar issues under Section 14(e).

The Court has also agreed to determine the standard of culpability necessary to sustain an action for damages against a professional under Section 10(b) in *Ernst & Ernst* v. *Hochfelder, cert. granted,* 95 S. Ct. 1557. The same determination should also be made with respect to Section 14(e), and this is an appropriate case for that purpose, involving as it does, only judgments made in good faith with which an appellate court later disagreed (A158-159).

II.

The Magnitude of Damages Assessed Against First Boston Contravenes the Express Intent of Congress.

While utilizing Section 11 of the 1933 Act to find First Boston liable, the Court of Appeals ignored the express

damage limitations and causation principles prescribed in that statute.

Section 11 as originally enacted contained both the standard of "absolute liability" commonly known as the duty of due diligence, and a rescission measure of damages such as that utilized by the Court of Appeals. In passing the 1934 Act, however, Congress amended Section 11 to limit the damage exposure of underwriters in two significant aspects:

> 1. Damages may not include any diminution in value not "resulting from" a breach of the underwriter's duty, and
>
> 2. The liability of an underwriter is limited to the "total price at which the securities underwritten by him and distributed to the public were offered to the public".

15 U.S.C. § 77k(e).

Section 11's requirement that there be a causal nexus between the violations and the damages asserted would absolutely preclude the rescission measure of damages adopted by the Court of Appeals. Congress enacted the amendment to Section 11 specifically to avoid claims for damages resulting from a general market decline. *See* 78 Cong. Rec. 10185-86 (June 7, 1934).

The Court of Appeals, citing *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, held that the fact that Bangor Punta Corporation might not have gained control of Piper without making the exchange offer was sufficient proof that the deficiency in the registration statement prepared in connection with the exchange offer "caused" Chris-Craft to

lose the contest and to suffer huge "damages" as the market value of Piper shares later declined. *Mills* supports no such proposition, and the Court of Appeals' mischaracterization of it contravenes the express causation requirement of Section 11.[2]

Under Section 11, moreover, First Boston's maximum possible liability for damages, assuming causation in fact, was "the total price" of the securities "distributed to the public," which was approximately $8,000,000. The award of $35,000,000 totals over *four times* the total price of the securities underwritten by First Boston.

III.

A Dealer Manager in an Exchange Offer Should Not Be Held Jointly and Severally Liable for Separate and Independent Violations of Law by its Principal and Other Defendants.

The Court of Appeals held that First Boston had violated the securities laws only with respect to its conduct as a dealer manager in the exchange offer to the Piper shareholders. Yet First Boston was held jointly and severally liable with its principal and the other defendants for various other purported violations of the securities laws they were found to have committed. For example, First Boston did not participate in its principal's purchase of 120,200 shares of Piper stock which the Court of Appeals held

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[2] Recognizing the detrimental effects of assuming causation for damages in an action where the defendant has not acted fraudulently or in bad faith, the SEC has taken the position that, in such circumstances, a clear nexus between any claim for damages and alleged violations must be shown. Brief for the Securities and Exchange Commission as *Amicus Curiae, Ernst & Ernst* v. *Hochfelder,* No. 74-1042, at 8-9.

violated Rule 10b-6 under the 1934 Act. The Court found that the acquisition of those shares was an essential step in obtaining control of Piper.

In *White* v. *Abrams,* 495 F.2d 724 (9th Cir. 1974), the Ninth Circuit suggested that with respect to actions under the 1934 Act a flexible duty standard should be applied in determining liability in an action involving multiple defendants. Under this approach the Court considers a number of factors, including benefit to the defendant, reliance, and who had initiated the transaction. The equitable considerations underlying it apply with special force to a determination of damages against parties in the position of First Boston.

Investment bankers in tender offer situations usually play a secondary role and the overall battle for economic control may rage on many other fronts of which the banker may have little, if any, knowledge. The trial court found that First Boston had played such a secondary role here and the Court of Appeals affirmed that finding.[3] The limited interest of First Boston in the entire matter was its $40,000 dealer manager's fee which was based on its services as a dealer manager. The record shows it had no substantive

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[3] The Court of Appeals stated at footnote 25 of its opinion on liability:

> "We agree with the district court that there is no merit to CCI's [Chris-Craft's] other claims against First Boston, essentially that it was the chief strategist for Piper and BPC in the control battle. The district court found, based on substantial evidence, that in its capacity as investment banker First Boston merely provided professional services to these companies. The business decisions that led to violations of the securities laws were initiated by these companies, not by First Boston in its role as investment banker. We are aware of no authority for holding First Boston liable in that capacity." (A55)

decision making power (A55). First Boston was not held to have acted with fraudulent intent or for the purpose of causing injury in any way to Chris-Craft in failing to make the particular disclosure involved.

We submit that in such circumstances the imposition of joint liability upon First Boston for all damages held to have been suffered by Chris-Craft is inequitable and totally unnecessary to effective enforcement of the securities laws.

CONCLUSION

For the reasons stated, First Boston's petition for a writ of certiorari to the Second Circuit Court of Appeals should be granted.

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